SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1933

No. 937

THE COLUMBUS GAS AND FUEL COMPANY,
Appellant,

vs.

THE PUBLIC UTILITIES COMMISSION OF OHIO AND THE CITY OF COLUMBUS, OHIO,
Appellees.

MEMORANDUM OF APPELLEE, THE CITY OF COLUMBUS.

Statement.

In oral argument of this cause counsel was requested by the Court to file certain memoranda setting forth information and record references which at the moment could not be supplied. Counsel was also granted leave to file other memoranda.

This brief memorandum is being filed in accordance with our understanding in the premises.

The Logan Gas Company Purchase.

On June 1, 1929, The Logan Gas Company was acquired by The Ohio Fuel Gas Company (R. p. 896). The purchase price was 441,252 shares of the common stock of The Ohio Fuel Gas Company—par value $50.00 each—(R. p. 1469). Even prior to the date of actual purchase, The Logan Gas Company was being operated by The Ohio Fuel Gas Company (R. pp. 1037, 1038) and at the time of the purchase both The Logan Gas Company and The Ohio Fuel Gas Company were controlled by The Columbia Gas and Electric Corporation (R. pp. 1468, 1472), so that the purchase was made between affiliated companies and was not an arm's length transaction.

The Arbitrary Write-Up.

During the year 1919 The Logan Gas Company by an arbitrary write-up of $3,748,036.48 increased its book account of leaseholds from $2,453,526.38 to $6,201,662.86 (R. pp. 1462, 1463, 196).

Depreciation of Gas Well Construction and Equipment.

In the course of oral argument counsel for the City of Columbus stated that the assertion of counsel for the Columbus Company in his argument to the Court, that the Supreme Court of Appeals of West Virginia reversed the Commission in its finding for gas well depreciation in *City of Charleston et al.*, v. *Public Service Commission,* 110 W. Va. 245, was incorrect.

The Supreme Court of Appeals for West Virginia only suggested that the Public Service Commission of West Virginia review the evidence "and unless there is a sufficient number of old wells to offset the new wells, then the value of the equipment be adjusted in some more uniform manner." The Public Service Commission of West Virginia, when the case was remanded to it, did not find it necessary to disturb the former depreciation based upon decline in rock pressure and the rates charged by the United Fuel Gas Company at present in the territory involved in that case are based upon that finding.

It will be recalled that the record in the matter of the United Fuel Gas Company is a part of the record in this case.

The opinion of the Commission, which was written after the case was remanded, is reported in P. U. R. 1932, B. 61.

Annual Depreciation Charge, Including Depletion of Wasting Assets.

During oral argument counsel for the Company stated that no allowance was recognized by the Supreme Court of

Ohio for depletion of wasting assets. He indicated that the only annual charge approved is that of 1½% of the present value of depreciable property allowed by the Majority Commission amounting to $667,612.00. This is contrary to the statement made in brief in behalf of the Company, No. 937, pp. 7-8, where counsel admits that the court below approved the minority commission allowance of $1,765,607.00.

Counsel for the City was asked in the course of argument whether the Court in its opinion made any allowance for wasting assets. We are not certain whether the question was answered with sufficient clarity.

Our views are presented rather fully at pp. 215-218, of our brief in behalf of the city. It is there pointed out that the opinion of the minority commissioner took into account the experience of the Company, of existing depreciation reserve, and of necessary depreciation including depletion. As we understand the opinion of the Court the allowance of the minority commissioner in this matter was approved, as against the majority finding. The minority commissioner said:

> "I have, in computing an allowance for depreciation and amortization, used 2½% of the value of the property, excluding land, working capital and material and supplies, which reduces the amount claimed by the company in the sum of $5,103,855.00. A complete study has been made of the depreciation charges of the company which show for the year 1929, an unexpended depreciation reserve in the sum equal to 22.20% of the book value of the company's property.
>
> "It is my opinion, therefore, that an allowance of 2½% on the value of the property of The Ohio Fuel Gas Company is a reasonable allowance for depreciation in view of the fact that there has been allowed completely the company's figures for maintenance, including non-productive well drilling expense.

"These amount are sufficient, when taken together, to maintain the property in a high standard of efficiency and to provide a reserve to take care of the property as it wears out and to utimately provide for the complete replacement of the property.

"The amount of depreciation, herein allowed, applicable to the portion of its property considered in this case is substantially the same amount in dollars, as shown by the books of the company for its entire properties, including its distribution system" (R. 205).

The annual allowance thus arrived at by Commissioner Bricker was $1,765,607.00 (R. 217). It provides for all properties including wasting assets.

As of December 31, 1929, the accumulated depreciation reserve of Ohio Fuel was $20,745,566.55, and on December 31, 1930, it stood at $21,011,147.43, without addition of accumulated interest (R. 2902, 3034). The surplus of the Company as of December 31, 1929, was $5,288,031.10 (R. 2902).

In our brief, pp. 204-213, we have set forth a careful explanation of the mistake of the majority commission in spreading amortization for gas wells and leaseholds over a period of three years and two months, instead of spreading it over 6.4 years, as the facts demand.

We have indicated at page 211 of our brief the difference in the gate charge to the Columbus Company resulting from a correction of the error. This results in an approximate reduction of 4 cents per M c. f.

If the amount found by the minority commission, which amount opposing counsel concede was approved by the court, *supra*, be used, the cost of gas to the Columbus Gas & Fuel Company will be reduced 5.71¢ per M c. f.

This is arrived at by deducting $1,765,607 from $4,826,566, the total erroneous annual allowance provided for by the majority commission for depreciation and amortization, and dividing the result by 53,569,575, the annual M c. f. sales of Ohio Fuel Gas Company.

In the *Dayton Power and Light Company* v. *Public Utilities Commission of Ohio*, decided April 30, 1934, Mr. Justice Cardozo said:

> "The amount of the allowance is adequate and even liberal. It was made on the assumption (1) that the value of the gas fields in class No. 1 was $25 an acre, and (2) that the life expectancy of the contents of the wells and of the appurtenant structures and equipment was only three years and two months. Both assumptions are erroneous, though the error results to the appellant's benefit. As to assumption (1), the State court has held that there is no satisfactory evidence of the value of the leases in class No. 1 in excess of the value assigned to them upon the books. A depletion allowance must therefore be excessive if it is made in the belief that a value of $25 per acre is the amount to be restored. As to assumption (2), there has been an underestimate of the life expectancy of the gas content of the wells, resulting once more in an exaggerated allowance for inroads upon capital. The prediction may have been correct in respect of the wells already driven and in use, though this is far from certain, but it was certainly too low if expectancy is to be measured by sources of supply in the 291,000 acres that had never been tapped and were available for the future.
>
> "The effect of these errors, and indeed of the first of them alone, without attempting to estimate the consequences of the second, is to make the amortization charge excessive to the extent of $761,098.50. In figuring the charge the present value of the leases was treated as 41.8874 per cent of $7,284,900, or $3,051,455; that of the gas well construction as $5,944,692, and that of the gas well equipment as $4,069,434, a total of $13,065,581. The actual present value of the leases in class No. 1 was not more than 41.8874 per cent of $1,569,479, or $657,414. The fund to be restored through amortization was thus over-estimated to the extent of $2,394,041, or 18-3/10 per cent, which would reduce the annual charge, without change of the life

expectancy, from $4,158,954 to $3,397,865.50" (Pp. 9-10).

Subtracting $2,394,041 from $13,065,581 and dividing the result, $10,671,540 by 6.4, the corrected life expectancy of existing gas wells, on this basis we find the annual depreciation allowance for depletion to be $1,667,428. This is in addition to the annual allowance for depreciation only which was made by the majority commission.

The gate cost of 39¢ per M c. f. found by the majority commission included an annual allowance of $667,612.00 for depreciation alone and $4,158,954.00 for amortization. The effect of the errors of the majority commission in respect to the amortization figure, as shown above in the language of this Court in the Dayton Power and Light Case, is to reduce the amortization allowance from $4,158,954.00 to $1,667,428.00. This causes a reduction in the gate cost of gas to Columbus of 4.65¢ per M c. f. conceding for the moment that the majority commission finding is correct in all other respects, including the 1½% annual allowance for depreciation only, which we say, most emphatically, in light of the accumulated depreciation reserve and history of Ohio Fuel is too high.

Leaseholds.

Adjustment of the value of leaseholds from the arbitrary finding of the Commission to book value as shown by the Record, reduces the cost of gas at the City Gate .69¢ per M c. f.

The Cost of United Fuel Gas.

That the decision of the lower court in approving the minority commissioner's finding as to the proper cost of United Gas to Ohio Fuel makes 1.22¢ per M c. f. difference in the rate for the city has been stated by counsel for both the company and the city.

Allocation—(Apportionment).

In its opinion relative to this subject, the Supreme Court of Ohio said:

> "The court is impressed with the fact that in this State, the unit established by the Constitution for dealing with public utility service is the municipality. Article XVIII, Sections 4 and 5" (R. 60).

And it further held:

> "Just why the city of Columbus should be charged for the pipe lines extending to Indiana, to Toledo, and to Cincinnati, we cannot understand. By the preponderance of the evidence, the transmission lines north and northeast of Columbus do not contribute to the Columbus gas supply, and the gas rate in Columbus should not share any part of the cost, maintenance or depreciation of these lines. The test is what portion of the wells, the compressor stations, and the pipe lines is devoted to each city or community, and the method of allocation adopted by the majority and the minority of the Commission was erroneous. If the proper method of allocation had been adopted, the gate rate found would have been materially decreased.
>
> "We hold that the unit of allocation in this case is not the system, but the locality, and quoting Judge Hickenlooper, *supra*, that 'production expenses and valuation, general property valuation, general expenses, and working capital should be apportioned on the proportionate sales basis, transmission, system valuation, and expenses upon the demand mileage basis, and distribution upon actual valuation of the distribution plants in the several municipalities and actual expenses there incurred'" (R. 61, 62).

In declaring the law of Ohio in this matter, as demanded by our constitutional and legislative requirements, and in stating that, "If the proper method of allocation had been adopted, the gate rate found would have been materially decreased," since the methods and computations of the

City were the only facts before the Court and must necessarily have been those upon which the Court's conclusion is based, the Court must have approved the City's contentions and computations as to the difference in rates produced by the application of the City's methods.

Counsel for the City was requested to present a statement showing from the Record the effect of the application of demand mileage allocation factors contended for by the City in this case and their effect on the cost of gas at the Columbus gate when applied to the findings of the majority commission.

'Complying with this request, we are submitting the following statement which shows the reduction in the gate cost to the City of Columbus to be 6.8¢ per M c. f.

EXHIBIT "B" (R. 179)

The Columbus Gas & Fuel Company—Formal Case No. 5935

The Ohio Fuel Gas Company—Gate Rate

(Over)

Valuation:		Portion Applicable to Cols. Gas & Fuel Co. on M. C. F. Sales Basis	Allocation Percentages from City Exhibit No. 115 Page 11— Printed Record, Pages 3179 and 3180	Property and Expenses Allocable to Gas Use in Columbus Area, Using Commission Finding of Property and Expenses and Demand Mileage Allocation
Property devoted to the service of Columbus, Ohio, and other cities in Ohio and Indiana, exclusive of Distribution System property and the proportion of General Property applicable thereto, as of 12-31-29.				
Production System	$13,140,755	$1,460,559	17.1501	$2,253,653
Transmission System	42,404,329	4,713,123	10.2782	4,358,402
General Property	1,089,344	121,078	11.0746	130,445
General Overheads	7,928,820	881,266	(1)	943,950
Total Physical Property	64,563,248	7,176,026	.....	7,686,450
Leaseholds	7,284,900	809,696	17.1501	1,249,368
Working Capital and Materials and Supplies	2,690,132	299,001	16.8338	452,851
Total Property Used and Useful	74,538,280 A	8,284,723	.....	9,388,669

Expenses and Return on Investment:				
Proportion applicable to above Property for 1929.				
Purchased Gas—from U. F. G. Co. @ 22.04¢ per M. F. C.	3,413,162	379,363	17.1501	585,361
Purchased Gas—from Others	2,873,056	319,332	17.1501	492,732
Purchased Gas Expense	89,747	9,975	17.1501	15,392
Production Expenses	1,288,588 B	143,223	17.1501	220,994
Non-Productive Well Drilling Expenses	618,789	68,777	17.1501	106,123
Transmission Expenses	1,401,668 B	155,792	10.2782	144,066
General Administrative Expenses	391,979 B	43,567	12.9331	50,695
Other General Expenses	199,347 B	22,157	12.9331	25,782
Taxes	1,742,310 B	193,653	12.9331	225,335
Credits	782,358 *	86,957 *	12.9331	101,183 *
Depreciation and Amortization	4,826,566	536,459	12.9331	624,225
Return @ 6½%	4,844,988	538,507	(2)	610,263
Total Expenses and Return	20,907,842	2,323,848	.....	2,999,785
M. C. F. of Gas Sold:				
Proportion applicable to the above property for 1929	53,579,575	5,955,221	9,279,605 (3)	.....
Gate Rate per M. C. F.:				
Derived by dividing the Total Expenses and Return by the Total M. C. F. of Gas Sold	39.02¢	39.02¢	.....	32.22

DIFFERENCE DUE TO ALLOCATION 6.8 cents per M. C. F.

NOTE:

A. Detail of Valuation shown on Sheet 2.
B. Detail of Expenses shown on Sheets 3 and 4.
* In red ink.

(1) 14% of Property.
(2) 6½% of Allocated Property.
(3) Total in Columbus Area.

In connection with the subject of allocation, the contention is made by the company that had the distance of the travel of gas from Ravenswood, West Virginia, to Wheeler Compressor Station, been considered, the allocation factor to the City of Columbus would have increased from 10.2782 to 25.1395 (Company supplemental brief, p. 67).

Columbus receives only a fraction of this gas coming from the United in West Virginia, yet the Company in this contention figures the burden of the whole cost to Columbus alone. Manifestly, there is no justification for such a computation.

The witness Carter was cross-examined in this matter as follows:

> "Q. Did you put that 65 miles on any other users or user than Columbus?
>
> "A. No, sir, I did not.
>
> "Q. Why not?
>
> "A. Because I was attempting to show what effect such a procedure would have on the Columbus figure by changing the one and only figure" (R. 2069).

Conclusion.

Counsel for the City have not interpreted the Court's request and leave for the filing of memoranda as including the right to file a supplemental brief and we have, therefore, confined ourselves accordingly.

Respectfully submitted,

JOHN L. DAVIES,
City Attorney,
JAMES W. HUFFMAN,
Special Counsel,
Counsel for the City of Columbus, Ohio.

May 3, 1934.